

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF MICHIGAN  
SOUTHERN DIVISION

IN RE: CITY OF DETROIT, . Docket No. 13-53846  
MICHIGAN, .  
 . Detroit, Michigan  
 . December 3, 2013  
Debtor. . 10:00 a.m.  
. . . . .

HEARING RE. BENCH OPINION RE. ELIGIBILITY  
BEFORE THE HONORABLE STEVEN W. RHODES  
UNITED STATES BANKRUPTCY COURT JUDGE

APPEARANCES:

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1 THE CLERK: All rise. Court is in session. Please  
2 be seated. Case Number 13-53846, City of Detroit, Michigan.

3 THE COURT: Counsel, would you like to put your  
4 appearances on the record, please?

5 MR. HEIMAN: David Heiman, Jones Day, on behalf of  
6 debtors, and with me today are Bruce Bennett and Heather  
7 Lennox and Bob Hertzberg as well.

8 MR. HOWELL: Good morning, your Honor. Steven G.  
9 Howell, Dickinson Wright, special assistant attorney general,  
10 appearing on behalf of the State of Michigan.

11 MR. MONTGOMERY: Good morning, your Honor. Claude  
12 Montgomery of Dentons, and with me are Carole Neville and Sam  
13 Alberts from Dentons and Matt Wilkins as local counsel.

14 MR. PLECHA: Good morning, your Honor. Ryan Plecha  
15 from Lippitt O'Keefe on behalf of the retiree association  
16 parties.

17 MS. LEVINE: Good morning, your Honor. Sharon  
18 Levine, Lowenstein Sandler, for AFSCME.

19 MR. GORDON: Good morning, your Honor. Robert  
20 Gordon of Clark Hill on behalf of the Detroit Retirement  
21 Systems.

22 MS. PATEK: Good morning, your Honor. Barbara Patek  
23 of Erman, Teicher, Miller, Zucker & Freedman, and with me are  
24 Craig Zucker and Earle Erman on behalf of Detroit public  
25 safety unions.

1 MS. BRIMER: Good morning, your Honor. Lynn M.  
2 Brimer appearing on behalf of the Retired Detroit Police  
3 Members Association. With me this morning are Meredith Taunt  
4 and Mallory Field.

5 THE COURT: The Court decided to provide this  
6 summary of its written opinion, which it will issue shortly,  
7 because it is important to give the people of the City of  
8 Detroit the best opportunity to understand what the Court is  
9 ruling and why. I would not call this a brief summary. It's  
10 a bit extended, so settle in, please. The written opinion  
11 will be over 140 pages, and it will address in more detail  
12 and with more legal and factual support all of the arguments  
13 that have been made regarding eligibility. I thought this  
14 summary would be more accessible. It is critical to the  
15 process, indeed, to any judicial process, that those who are  
16 impacted by the Court's ruling have confidence that they were  
17 heard and that their arguments and concerns were fully and  
18 fairly considered.

19 The matter is before the Court on the parties'  
20 objections to the eligibility of the city to be a debtor in  
21 this Chapter 9 case under Section 109(c) of the Bankruptcy  
22 Code. The City of Detroit was once a hard-working, diverse,  
23 vital city, the home of the automobile industry, proud of its  
24 nickname, The Motor City. It was rightfully known as the  
25 birthplace of the American automobile industry. In 1952, at

1 the height of its prosperity and prestige, it had a  
2 population of 1,850,000 residents. It was building half of  
3 the world's cars.

4 The evidence establishes, however, that for decades  
5 the City of Detroit has experienced dwindling population,  
6 employment, and revenues. This has led to decaying  
7 infrastructure, excessive borrowing, mounting crime rates,  
8 spreading blight, and a deteriorating quality of life. The  
9 city no longer has the resources to provide its residents  
10 with basic police, fire, and emergency medical services that  
11 its residents need for their basic health and safety. To  
12 reverse this decline in basic services and to attract new  
13 residents and businesses and to revitalize and reinvigorate  
14 itself, the city needs help.

15 The city estimates that its debt is \$18 billion.  
16 This consists of 11.9 billion in unsecured debt and 6.4  
17 billion in secured debt. It has more than 100,000 creditors.  
18 According to the city, this unsecured debt includes \$5.7  
19 billion for other post-employment benefits through June of  
20 2011, which is the most recent actuarial data available; 3.5  
21 billion in unfunded pension obligations; \$650 million in  
22 general bond obligations; \$1.43 billion for certificates of  
23 participation related to the pensions; \$346.6 million for  
24 swap contracts, liabilities related to the certificates of  
25 participation; and \$300 million of other liabilities. Except

1 for the unfunded pension liability, the parties -- the  
2 objecting parties do not seriously challenge the city's  
3 estimates of this debt. The pension plans and others have  
4 suggested a much lower pension underfunding amount, perhaps  
5 even below \$1 billion. However, the Court concludes that it  
6 is not necessary to resolve this issue at this time.  
7 Otherwise, the Court is satisfied that the city's estimates  
8 of its other liabilities are accurate enough for purposes of  
9 determining eligibility, and the Court so finds.

10 For the five years ending with fiscal year 2012,  
11 pension payments exceeded contributions and investment income  
12 by approximately \$1.7 billion for the General Retirement  
13 Systems and \$1.6 billion for the Police and Fire Retirement  
14 Systems. This, of course, resulted in the liquidation of  
15 pension trust principal.

16 Using current actuarial assumptions, the city's  
17 required pension contributions as a percentage of eligible  
18 payroll expenses are projected to grow from 25 percent for  
19 the GRS and 30 percent for the PFRS in 2012 to 30 percent for  
20 the GRS and 60 percent for the PFRS by 2017. Changes in  
21 actuarial assumptions would further increase the city's  
22 required pension contributions. During 2012, 39 percent of  
23 the city's revenue was used to service legacy liabilities.  
24 The forecasts for subsequent years, assuming no  
25 restructuring, are 43 percent for 2013 going up to 65 percent

1 for 2017.

2           The Court will now address the transactions referred  
3 to as the certificates of participation, often called the  
4 COP's, and the swaps associated with them. These  
5 transactions are complex and confusing, and so is the  
6 resulting litigation. The Court will provide only the  
7 briefest summary of them at this time.

8           In 2005 and 2006, the city decided to raise \$1.4  
9 billion for its underfunded pension funds. A substantial  
10 part of this funding was at an interest rate that would float  
11 with the market. If the market interest rate went up, so did  
12 the rate on the COP's and vice versa. As part of the  
13 transaction, therefore, the city decided to try to protect  
14 itself against interest rates going up, so it entered into a  
15 wager. The more common name for this is a swap, but it's  
16 nothing more than a common bet. If the rate went up, someone  
17 would pay the city to help cover the increased interest  
18 expense. If the rate went down, the city would have to pay.  
19 In 2008 interest rates dropped dramatically. As a result,  
20 the city lost on the swaps bet. Actually, it lost  
21 catastrophically on the swaps bet. The city estimates that  
22 the damage will be approximately \$45 million per year for the  
23 next ten years. The result has been complex and expensive  
24 litigation. In any event, the city estimates that as of June  
25 30, 2013, it may owe \$480 million from the 2005 COP's and



1 \$949 million on the 2006 COP's. It also has a potential  
2 liability in excess of \$300 million on the swaps, although  
3 the city has serious and substantial challenges to those  
4 amounts.

5 Debt service from the city's general fund related to  
6 limited tax and unlimited general obligation debt and the  
7 COP's was \$225 million for fiscal year 2012 and is projected  
8 to exceed \$247 million in 2013. The city estimates that 38  
9 percent of tax revenues go to debt service rather than city  
10 services. It further estimates that without changes, this  
11 will increase to 65 percent within five years. At the same  
12 time, however, tax revenues are going down. State revenue  
13 sharing is also going down. It has decreased by \$161  
14 million, 48 percent, since 2002 and by \$67 million, 31  
15 percent, since 2008.

16 The city has experienced large operating deficits  
17 for each of the past seven years. Through 2013, it has an  
18 accumulated general fund deficit of \$237 million. However,  
19 this includes the effect of recent debt issuances. The city  
20 borrowed \$75 million in 2008, \$250 million in 2010, and \$129  
21 million in 2013. If the city had not borrowed these amounts,  
22 the city's accumulated general fund deficit would have been  
23 \$700 million through 2013. In 2012, the city had a negative  
24 cash flow of \$115 million excluding the proceeds from  
25 borrowings. In March of 2012, to avoid running out of cash,

1 the city borrowed \$80 million. In 2013, the city deferred  
2 payments on certain of its obligations totaling \$120 million  
3 for current and prior year pension contributions and other  
4 payments.

5 Absent restructuring, the city projects it will have  
6 negative cash flows of \$190 million for 2014 increasing to  
7 \$346 million for 2017. The city further estimates that by  
8 2017 its accumulated deficit will grow to approximately \$1.3  
9 billion. The city is not making its pension contributions as  
10 they become due. As of May 2013, the city had deferred  
11 approximately \$54 million in pension contributions and  
12 approximately \$50 million on June 30th, 2013, for current  
13 year pension contributions.

14 Also, the city did not make the scheduled \$39.7  
15 million payment on its COP's that were due on June 14, 2013.  
16 If the city had not deferred these payments, it would have  
17 run out of cash by June 30th, 2013. Let me repeat that. If  
18 the city had not deferred these payments, it would have run  
19 out of cash by June 30th, 2013. It filed for bankruptcy 18  
20 days later.

21 The city will -- the Court will now review the  
22 causes and consequences of this. These are discussed  
23 together because it can be hard to tell which is a cause and  
24 which is a consequence. Detroit's population declined to  
25 684,800 in December of 2012. This is a 63-percent decline in

1 population from its peak in 1950. In June 2000, Detroit's  
2 unemployment rate was 6.3 percent. In June 2010, it was 23.4  
3 percent. In June 2012, it was 18.3 percent. The number of  
4 employed Detroit residents fell from approximately 353,000 in  
5 2000 to 280,000 in 2012.

6 The city's credit ratings are below investment  
7 grade. In calendar year 2012, 136,00 crimes were reported in  
8 the city. Of these, 15,200 were violent crimes. The city's  
9 case clearance rate for violent crimes is 18.6 percent. The  
10 clearance rate for all crimes is 8.7 percent. These rates  
11 are substantially below those of comparable municipalities  
12 nationally and surrounding local communities.

13 As of April 2013, about 40 percent of the city's  
14 88,000 streetlights were not working. There are  
15 approximately 78,000 abandoned and blighted structures in the  
16 city. Of these, 38,000 are considered dangerous buildings.  
17 The city experiences 11 to 12,000 fires each year for the  
18 past decade. Approximately 60 percent of these were in  
19 blighted or unoccupied buildings. In 2012 the average  
20 priority one response time for the police department was 30  
21 minutes. In 2013 it was 58 minutes. The national average is  
22 11 minutes. The police department staffing has been reduced  
23 by approximately 40 percent over the last ten years. It has  
24 not invested in or maintained its facility infrastructure for  
25 many years and has closed or consolidated many precincts. It

1 operates with a fleet of 1,291 vehicles, most of which have  
2 reached the replacement age of three years and lack modern  
3 information technology. The average age of the city's 35  
4 fire stations is 80 years. The fire department's fleet has  
5 many mechanical issues, contains no reserve vehicles, and  
6 lacks equipment ordinarily considered standard. During the  
7 first quarter of 2013, frequently only ten to fourteen of the  
8 city's 36 ambulances were in service. The city's information  
9 technology infrastructure and software is obsolete and is not  
10 integrated between departments or even within departments.  
11 The city has reduced the number of its employees by about  
12 2,700 since 2011. As of May 31st, 2013, it has approximately  
13 9,560 employees.

14           The city's union employees are represented by 47 or  
15 48 discrete bargaining units. The collective bargaining  
16 agreements covering all of these bargaining units expired  
17 before the case was filed. The city has implemented revised  
18 employment terms called City Employment Terms for  
19 nonunionized employees and for unionized employees under  
20 expired collective bargaining agreements.

21           It has also increased revenues and reduced expenses  
22 in other ways. It estimates that these measures have  
23 resulted in annual savings of \$200 million. The city cannot  
24 legally increase its tax revenues nor can it reduce its  
25 employee expenses without further endangering public health

1 and safety.

2 Before reviewing the events leading to the filing of  
3 this case, a brief review of the winding history of the  
4 Michigan statutes on point is necessary. In 1990 the  
5 Michigan legislature enacted Public Act 72 of 1990, the Local  
6 Government Fiscal Responsibility Act. This act empowered the  
7 state to intervene with respect to municipalities that faced  
8 financial crisis through the appointment of an emergency  
9 financial manager, who would assume many of the powers  
10 ordinarily held by local public officials. Effective March  
11 16, 2011, PA 72 was repealed and replaced with Public Act 4  
12 of 2011, the Local Government and School District Fiscal  
13 Accountability Act. On November 5th, 2012, however, the  
14 Michigan voters rejected PA 4 by referendum. In Davis v.  
15 Roberts, the Michigan Court of Appeals held that this  
16 rejection revived Public Act 72. Public Act 72 remained in  
17 effect until March 28, 2013, when Public Act 436, the Local  
18 Financial Stability and Choice Act, became effective. The  
19 legislature had enacted that law on December 13, 2012, and  
20 the governor had signed it on December 26, 2012.

21 On February 19, 2013, a financial review team  
22 appointed by the governor submitted its report regarding the  
23 city. That report concluded that a local government  
24 financial emergency exists within the City of Detroit because  
25 no satisfactory plan exists to resolve a serious financial

1 problem. On March 1st, 2013, after receiving that report,  
2 the governor announced his determination that a financial  
3 emergency existed within the city. On March 12, 2013,  
4 Governor Snyder conducted a public hearing to consider the  
5 City Council's appeal of his determination. On March 14,  
6 2013, the governor confirmed his determination of a financial  
7 emergency within the city and requested that the Local  
8 Emergency Financial Assistance Loan Board appoint an  
9 emergency financial manager under PA 72. On March 15, 2013,  
10 the Loan Board appointed Kevyn Orr as the emergency financial  
11 manager for the City of Detroit. On March 15, Mr. Orr took  
12 office formally. On March 18, which was the effective date  
13 of PA 436, PA 72 was repealed, and Mr. Orr became the  
14 emergency manager of the city under PA 436.

15 Under law, the emergency manager acts for and in the  
16 place and stead of the governing body and the office of the  
17 chief administrator -- administrative officer of the local  
18 government. He has broad powers in receivership to rectify  
19 the financial emergency and to assure the fiscal  
20 accountability of the local government and the local  
21 government's capacity to provide or cause to be provided  
22 necessary government services essential to the public health,  
23 safety, and welfare.

24 On June 14, 2013, Mr. Orr organized a meeting with  
25 approximately 150 representatives of the city's creditors.

1 Mr. Orr presented the June 14 creditor proposal, Exhibit 43,  
2 and answered questions. At the conclusion of the meeting,  
3 Mr. Orr invited creditor representatives to provide feedback  
4 to the city regarding the proposal. This proposal described  
5 the economic circumstances that resulted in Detroit's  
6 financial condition. It also offered a restructuring of the  
7 city's operations, financing, and capital structure. It also  
8 offered recoveries for each creditor group.

9           Regarding creditor recoveries, the city proposed,  
10 (a) treatment of secured debt adequate to the value of the  
11 collateral; (b) the pro rata distribution of \$2 billion in  
12 principal amount of interest only limited recourse  
13 participation notes to holders of unsecured claims -- that  
14 is, the unsecured bondholders, the COP's, the pension  
15 systems, retirees, and other unsecured claims -- and (c) a  
16 Dutch auction process for the city to purchase or pay the  
17 notes.

18           Following the June 14, 2013, meeting at which the  
19 proposal to creditors was presented, Mr. Orr and his staff  
20 had several other meetings. On June 3, 2013, two lawsuits  
21 were filed against the governor and the treasurer in state  
22 court. These suits sought a declaratory judgment that PA 436  
23 violated the Michigan Constitution to the extent that the law  
24 purported to authorize bankruptcy proceedings in which vested  
25 pension benefits might be impaired. The suits also sought an

1 injunction preventing the governor from authorizing a  
2 bankruptcy proceeding for the City of Detroit in which  
3 pension -- vested pension benefits might be impaired. The  
4 two cases were Flowers v. Snyder and Webster v. Snyder. On  
5 July 17, 2013, the GRS commenced a similar lawsuit, General  
6 Retirement System of the City of Detroit v. Orr. On the day  
7 before, July 16, 2013, Mr. Orr had recommended to the  
8 governor and the treasurer that the city file for Chapter 9  
9 relief. On July 18, Governor Snyder authorized the City of  
10 Detroit to file a Chapter 9 bankruptcy case. At 4:06 p.m. on  
11 July 18, 2013, the City of Detroit filed this Chapter 9  
12 bankruptcy case.

13           Before turning to the filed objections in this case,  
14 it is necessary to point out that the city bears the burden  
15 to establish by a preponderance of the evidence each of the  
16 elements of eligibility under Section 109(c). As the Court  
17 commented at the conclusion of the hearing on September 19,  
18 2013, the individuals' presentations on that day were moving,  
19 passionate, thoughtful, compelling, and well-articulated.  
20 These presentations demonstrated an extraordinary depth of  
21 concern for the City of Detroit, for the adequate level of  
22 services that their city government provides, and for the  
23 personal hardships that that creates, and most clearly for  
24 the pensions of the city retirees and employees. These  
25 individuals expressed another deeply held concern and even



1 anger that became a major theme of the hearing, the concern  
2 and anger that the state's appointment of an emergency  
3 manager over the City of Detroit violated their fundamental  
4 democratic right to self-governance.

5           The Court's role here is to evaluate how these  
6 concerns might impact the city's eligibility for bankruptcy.  
7 In making that evaluation, of course, the Court can only  
8 consider the specific requirements of applicable law. The  
9 popularity of the decision to appoint an emergency manager is  
10 not a matter of eligibility under the federal bankruptcy  
11 laws. The Court has carefully considered the concerns of the  
12 individuals that filed eligibility objections, including  
13 those that addressed the Court on September 19 of this year.  
14 Those concerns are addressed throughout the Court's opinion  
15 but are primarily addressed in the context of whether this  
16 case was filed in good faith.

17           The Court will now begin its findings and  
18 conclusions. The City of Detroit is a municipality as  
19 defined in the Bankruptcy Code. The parties agree to that.  
20 Several objecting parties challenge the constitutionality of  
21 Chapter 9 of the Bankruptcy Code under the United States  
22 Constitution. Citing the United States Supreme Court's  
23 decision in Stern versus Marshall, these parties also assert  
24 that this Court does not have the authority to determine the  
25 constitutionality of Chapter 9. Several objecting parties

1 also challenge the constitutionality of Public Act 436 under  
2 the Michigan Constitution. Some of these parties also assert  
3 that this Court does not have the authority to determine the  
4 constitutionality of PA 436.

5 The Official Committee of Retirees previously filed  
6 a motion to withdraw the reference to the District Court on  
7 the grounds that this Court does not have the authority to  
8 determine the constitutionality of either Chapter 9 or PA  
9 436. It also filed a motion for stay of the eligibility  
10 proceedings pending the District Court's resolution of that  
11 motion. In this Court's denial of the stay motion, it  
12 concluded that the committee was unlikely to succeed on its  
13 arguments regarding this Court's lack of authority under  
14 Stern. For the reasons stated in that opinion, the Court  
15 concludes that it has the authority to determine the  
16 constitutionality of Chapter 9 and PA 436.

17 The objecting parties argue that Chapter 9 of the  
18 Bankruptcy Code violates several provisions of the United  
19 States Constitution both on its face and as applied in this  
20 bankruptcy case. Article I, Section 8, of the United States  
21 Constitution provides the Congress shall have the power to  
22 establish uniform laws on the subject of bankruptcies  
23 throughout the United States. The objecting parties assert  
24 that Chapter 9 violates the uniformity requirement of the  
25 United States Constitution because Chapter 9 cedes to each

1 state the ability to define its own qualifications for a  
2 municipality to declare bankruptcy, and, therefore, Chapter 9  
3 permits the promulgation of nonuniform bankruptcies within  
4 the states. The Supreme Court has addressed the uniformity  
5 requirement in several cases. Most notably, in Hanover  
6 National Bank v. Moyses in 1902 the Supreme Court held that  
7 the incorporation into the bankruptcy law of state laws that  
8 relate to exemptions did not violate the uniformity  
9 requirement of the Constitution. The Court stated, "The  
10 general operation of the law is uniform although it may  
11 result in certain peculiarities differently in different  
12 States" -- I'm sorry -- "certain particulars differently in  
13 different States."

14 The Court concludes that Chapter 9 does exactly what  
15 the Supreme Court cases require to meet the uniformity  
16 requirement. The defined class of debtors to which Chapter 9  
17 applies is the class of entities that meet the eligibility  
18 requirements. One such class qualification is that the  
19 entity is specifically authorized to be a debtor under  
20 Chapter 9 by state law. As Moyes held, it is of no  
21 consequence in the uniformity analysis that this requirement  
22 of state authorization to file a Chapter 9 case may lead to  
23 different results in different states. Accordingly, the  
24 Court concludes that Chapter 9 satisfies the uniformity  
25 requirement of the bankruptcy clause of the United States

1 Constitution.

2           The contracts clause of the United States  
3 Constitution provides, quote, "No State shall pass any law  
4 impairing the Obligation of Contracts," close quote. It is  
5 argued that Chapter 9 violates the contracts clause. This  
6 argument is rejected. Chapter 9 is a federal law, not a  
7 state law. Article I, Section 10, does not prohibit Congress  
8 from enacting a law impairing the obligation of contracts.

9           The Tenth Amendment challenge to Chapter 9 is the  
10 most strenuously argued here. That amendment provides,  
11 quote, "The powers not delegated to the United States by the  
12 Constitution, nor prohibited by it to the States are reserved  
13 to the States respectively, or to the people," close quote.  
14 The objecting parties argue that Chapter 9 of the Bankruptcy  
15 Code violates the principles of federalism that are reflected  
16 in this amendment. The argument is that through Chapter 9,  
17 Congress has established rules that control state fiscal  
18 self-management, which is an area of exclusive state  
19 sovereignty. This argument is a facial challenge to the  
20 constitutionality of Chapter 9. The as applied challenge is  
21 that if the State of Michigan can properly authorize the City  
22 of Detroit to file for Chapter 9 relief without the explicit  
23 protection of pension rights for retired city employees, then  
24 Chapter 9 is unconstitutional because that would violate  
25 Michigan's sovereignty.

1           Before addressing the merits of these arguments,  
2           however, the Court must first address two preliminary issues  
3           that the United States raised, standing and ripeness. First,  
4           the Court concludes that the objecting parties do have  
5           standing. Section 1109(b) of the Bankruptcy Code provides,  
6           quote, "A party in interest, including a creditor, may raise  
7           and appear and be heard on any issue in a case under this  
8           chapter," close quote. Section 901(a) makes this provision  
9           applicable in a Chapter 9 case. Accordingly, the objecting  
10          parties who are creditors with pension claims against the  
11          city have standing to assert their constitutional challenges  
12          as part of their objections to this bankruptcy case.

13          The United States further argues that the issue of  
14          whether Chapter 9 is constitutional as applied in this case  
15          is not ripe for determination at this time. The city joins  
16          in this argument. Early on in this case, the Court expressed  
17          its own doubts about this thinking that the issue of whether  
18          pension rights can be impaired in bankruptcy applied more to  
19          confirmation than to eligibility. The Court finds now that  
20          these issues are ripe for decision. At the request of the  
21          objecting parties, the Court, therefore -- excuse me --  
22          reconsidered that position and now agrees that the issue is  
23          ripe at this point.

24          The premise of the argument that the United States  
25          makes is that the filing of the case did not result in the

1 impairment of any pensions, thus the United States argues  
2 that this issue will be ripe only when the city proposes a  
3 plan that would impair pensions if it were confirmed. Until  
4 then, it argues their injury is speculative. Although the  
5 argument of the United States has some appeal, as the Court  
6 itself initially concluded, the Court must now reject it.

7           The ultimate issue before the Court at this time is  
8 whether the city is eligible to be a debtor in Chapter 9.  
9 This dispute arises in the concrete factual context of the  
10 City of Detroit's filing this bankruptcy case under Chapter 9  
11 of the Bankruptcy Code and the objecting parties challenging  
12 the constitutionality of that very law. This dispute is not  
13 an abstract disagreement that is ungrounded in the here and  
14 now. It is here, and it is now. The Court further concludes  
15 that as a matter of judicial prudence resolving this issue  
16 now will likely expedite the resolution of this bankruptcy  
17 case. The parties have fully briefed and argued the merits.  
18 Further, if the Tenth Amendment challenge to Chapter 9 is  
19 resolved now, the parties and the Court can then focus on  
20 whether the Court -- whether the city's plan will meet the  
21 confirmation requirements of the Bankruptcy Code.  
22 Accordingly, the Court concludes that the objecting parties'  
23 challenge to Chapter 9 of the Bankruptcy Code as applied in  
24 this case is ripe for determination at this time.

25           The Court concludes that the United States Supreme

1 Court has already decided the question of whether a federal  
2 municipal bankruptcy act can be administered consistent with  
3 the principles of federalism reflected in the Tenth  
4 Amendment. In United States versus Bekins, the Supreme Court  
5 specifically upheld the Municipal Corporation Bankruptcy Act  
6 of 1937 over the objections that the statute violated the  
7 Tenth Amendment. It is well-settled that this Court is bound  
8 by the decisions of the United States Supreme Court.

9           Nevertheless, the objecting parties assert that  
10 Bekins is no longer good law because of amendments to the  
11 municipal bankruptcy statute after Bekins was decided and  
12 because of two more recent Supreme Court decisions regarding  
13 the Tenth Amendment. However, the Court concludes first that  
14 changes to the municipal bankruptcy law since 1937 have been  
15 minor and do not undermine the continuing validity of Bekins.  
16 Second, changes to the Supreme Court's Tenth Amendment law do  
17 not undermine the continuing validity of Bekins. In its  
18 recent cases deciding issues under the Tenth Amendment, New  
19 York versus United States and Printz versus United States,  
20 the Supreme Court has upheld laws that encourage states to  
21 regulate according to federal policies so long as the states  
22 consent. On the other hand, laws that compel or commandeer  
23 state resources do violate the Tenth Amendment. The key is  
24 state consent. Chapter 9 simply does not raise a consent  
25 issue. As the Supreme Court emphasized in Bekins, Chapter 9

1 is limited to voluntary proceedings. The federal government  
2 cannot and does not compel states to authorize municipalities  
3 to file for Chapter 9 relief, and municipalities are not  
4 permitted to seek Chapter 9 relief without specific state  
5 authorization. There is simply no commandeering or  
6 compulsion involved. Therefore, the Court concludes that  
7 Chapter 9 is not facially unconstitutional under the Tenth  
8 Amendment of the United States Constitution.

9           Several of the objecting parties also raise as  
10 applied challenges to the constitutionality of Chapter 9  
11 under the Tenth Amendment. The primary point of these  
12 arguments is that if Chapter 9 permits the State of Michigan  
13 to authorize a city to file a petition for Chapter 9 relief  
14 without explicitly providing for protection of  
15 constitutionally protected pension rights, then the Tenth  
16 Amendment is violated. The State of Michigan itself cannot  
17 legally provide for the adjustment of pension debts or any  
18 debts of the City of Detroit. That is so because the United  
19 States Constitution and the Michigan Constitution both  
20 prohibit the State of Michigan from impairing contracts. It  
21 is also because the Michigan Constitution prohibits the  
22 impairing of the -- of accrued pension benefits. These  
23 prohibitions, however, do not apply in the federal Bankruptcy  
24 Court. As the Bankruptcy Court in the City of Stockton  
25 Chapter 9 case said, the bankruptcy clause of the United



1 States Constitution necessarily authorizes Congress to make  
2 laws that would impair contracts, so it has long been  
3 understood that bankruptcy law entails impairment of  
4 contracts. For purposes of the Tenth Amendment and state  
5 sovereignty, nothing distinguishes pension debt in a  
6 municipal bankruptcy case from any other debt. If the Tenth  
7 Amendment prohibits the impairment of pension benefits in  
8 this case, then it would also prohibit the adjustment of any  
9 other debt in the case like bond debt. Bekins makes it  
10 clear, however, that with state consent the adjustment of  
11 municipal debts does not impermissibly intrude on state  
12 sovereignty. This Court is bound to follow that Supreme  
13 Court holding.

14           The plans and other objecting parties counter that  
15 result by asserting that under the Michigan Constitution  
16 pension debt has greater protection than ordinary contract  
17 debt. The argument is premised on the slim read that in the  
18 Michigan Constitution the pension clause provides that  
19 pension rights may not be, quote, "impaired or diminished"  
20 whereas the contracts clause in the Michigan Constitution  
21 only prohibits impairing contract rights. There are several  
22 reasons why the slight difference between the language that  
23 protects contracts, no impairment, and the language that  
24 protects pensions, no impairment or diminishment, does not  
25 demonstrate that pensions are entitled to any extraordinary

1 protection. At common law, before the adoption of the  
2 Michigan Constitution in 1963, public pensions in Michigan  
3 were viewed as gratuitous allowances that could be revoked at  
4 will because a retiree lacked any vested right in their  
5 continuation. In 1963, this new provision enhancing the  
6 protection for pensions was included, quote, "The accrued  
7 financial benefits of each pension plan and retirement system  
8 of the state and its political subdivisions shall be a  
9 contractual obligation thereof which shall not be diminished  
10 or impaired thereby," close quote. That's Article IX,  
11 Section 24, of the Michigan Constitution of 1963.

12 So here are the reasons why pension rights are  
13 contract rights under the Michigan Constitution. First, as  
14 noted, the language of Article IX, Section 24, gives pension  
15 benefits the status of a, quote, "contractual obligation,"  
16 close quote. That's the language that it uses.

17 Second, if the Michigan Constitution were meant to  
18 give the kind of higher or even absolute protection for which  
19 the plans argue here, that language simply would not have  
20 referred to pension benefits as a, quote, "contractual  
21 obligation," close quote.

22 Third, linguistically there is no functional  
23 difference in meaning between "impair" and "impair or  
24 diminish." Now, there certainly is a preference, if not a  
25 mandate, to give every -- to give meaning to every word in

1 written law. At the same time, however, we give undefined  
2 statutory terms their plain and ordinary meanings. If this  
3 Court gives these terms, "diminish" and "impair," their plain  
4 and ordinary meanings, those meanings would not be  
5 substantially different from each other. The terms are not  
6 synonyms, but they cannot honestly be given meanings so  
7 different as to compel the result that the plans now seek,  
8 the protection of pension rights in bankruptcy. "Diminish"  
9 adds nothing material to "impair." All diminishment is  
10 impairment, and "impair" includes "diminish."

11 Fourth, the argument for a greater protection is  
12 inconsistent with the Michigan Supreme Court's interpretation  
13 of this constitutional language in two cases, Kosa versus  
14 Treasury -- Treasurer of the State of Michigan and In re.  
15 Constitutionality of 2011 PA 38. In Kosa in 1980 the  
16 Michigan Supreme Court quoted the history from the  
17 Constitutional Convention regarding Article IX, Section 24.  
18 Several times that history refers to pension rights as  
19 contractual rights. The Court in Kosa also itself used  
20 contractual language when referring to pension rights. More  
21 recently in In re. Constitutionality of 2011 PA 38 in 2011,  
22 the Michigan Supreme Court stated, quote, "The obvious intent  
23 of Section 24, however, was to ensure that public pensions be  
24 treated as contractual obligations that, once earned, could  
25 not be diminished," close quote.

1 Fifth, an even greater narrative must be considered  
2 here focusing on 1963. At that time, Michigan law allowed  
3 municipalities to file a bankruptcy, and Bekins had long  
4 since held that that was constitutional, so when the new  
5 Michigan Constitution was negotiated and proposed and  
6 ratified in 1963, it explicitly gave accrued pension benefits  
7 only the status of contractual obligations. That new  
8 Constitution could have given pensions protection from  
9 impairment in bankruptcy in several ways, but it did not. It  
10 could have simply prohibited Michigan municipalities from  
11 filing bankruptcy. It could have somehow created a property  
12 interest that bankruptcy would be required to respect, or it  
13 could have established some sort of a secured interest in the  
14 municipality's property. It could have even required the  
15 state to guarantee pension benefits, but it did none of  
16 those. Instead, both the history from the Constitutional  
17 Convention and the very language of the pension provision  
18 itself, it is made clear municipal pension rights are  
19 contract rights. Because under the Michigan Constitution  
20 pension rights are contractual rights, they are subject to  
21 impairment in a federal bankruptcy proceeding. Moreover,  
22 where, as here, the state consents, that impairment does not  
23 violate the Tenth Amendment. Therefore, as applied in this  
24 case, Chapter 9 is Constitutional.

25 Nevertheless, the Court is compelled to comment. No

1 one should interpret this holding that pension rights are  
2 contract rights and subject to impairment in this bankruptcy  
3 case to mean that this Court necessarily will confirm any  
4 plan of adjustment that impairs pensions. The Court  
5 emphasizes that it will not lightly or casually exercise the  
6 power under federal bankruptcy law to impair pensions.  
7 Before the Court confirms any plan that the city submits, the  
8 Court must find that the plan fully meets the requirements of  
9 Section 943(b) of the Bankruptcy Code and the other  
10 applicable provisions of the Bankruptcy Code. Together these  
11 provisions of law demand this Court's judicious, legal, and  
12 equitable consideration of the interests of the city and the  
13 interests of all of its creditors, including retirees, as  
14 well as the laws of the State of Michigan.

15           Section 109(c)(2) of the Bankruptcy Code requires  
16 that a municipality be specifically authorized to be a debtor  
17 under such chapter. The evidence establishes that the city  
18 was authorized to file this case. The issue is whether that  
19 authorization was proper under the Michigan Constitution.  
20 Several objectors argue that the authorization is not valid  
21 because Public Act 436, the statute establishing the  
22 underlying procedure for a municipality to obtain  
23 authorization, is unconstitutional. The validity of Public  
24 Act 436 under the Michigan Constitution is a question of  
25 state law. The Michigan Supreme Court has not ruled on the

1 validity of Public Act 436. As a result, this Court must  
2 attempt to ascertain how that Court would rule if it were  
3 faced with this issue.

4 As discussed earlier, on March 16th, 2011, the  
5 governor signed Public Act 4 into law, but Public Act 4 was  
6 repealed by Public Act 72. However, the voters rejected  
7 Public Act 4 by referendum in the November 6, 2012, election.  
8 Shortly after that election on December 26th, 2012, the  
9 governor signed PA 436 into law, and it took effect on March  
10 28th, 2013. It is argued here that Public Act 436 is  
11 unconstitutional because it is essentially a reenactment of  
12 the rejected Public Act 4 in violation of the people's  
13 referendum rights. The city and the State of Michigan assert  
14 that there are several differences between Public Act 436 and  
15 Public Act 4 such that they are not the same law. In  
16 Reynolds versus Bureau of State Lottery in 2000, the Michigan  
17 Court of Appeals held that nothing in the Michigan  
18 Constitution suggests that a referendum has any broader  
19 effect than the nullification of the rejected act. This  
20 Michigan Court of Appeals decision strongly suggests that the  
21 referendum rejection of Public Act 4 did not prohibit the  
22 Michigan legislature from enacting Public Act 436 even though  
23 Public Act 436 addressed the same subject matter as Public  
24 Act 4 and did contain very few changes. Accordingly, the  
25 challenge on this ground must be rejected.

1           It is also contended that Public Act 436 is  
2     unconstitutional because the Michigan legislature included  
3     appropriations provisions in Public Act 436 for the sole  
4     purpose of shielding the act from referendum. There  
5     certainly was some credible evidence in support of the  
6     assertion that the appropriations provision in Public Act 436  
7     were intended to immunize it from referendum. For example,  
8     Howard Ryan, the legislative assistant in the Michigan  
9     Department of Treasury, so testified in his deposition. The  
10    Court must conclude, however, that if faced with this issue,  
11    the Michigan Supreme Court would not hold Public Act 436  
12    unconstitutional on this grounds. In Michigan United  
13    Conservation Clubs versus Secretary of State in 2001, the  
14    Court concisely held that a public act with an appropriations  
15    provision is not subject to referendum regardless of the  
16    motive of the appropriation. To the same effect was Houston  
17    v. Governor decided by the Michigan Supreme Court in 2012.  
18    Accordingly, the Court concludes that PA 436 is not  
19    unconstitutional on the grounds that the appropriations  
20    provisions of it improperly shielded it from the people's  
21    right of referendum.

22           Certain objectors also argue that Public Act 436  
23    violates the home rule provision of the Michigan  
24    Constitution, which recognizes the right of the electors to  
25    adopt and amend the city charter and the city's right to

1 adopt ordinances. The argument is that the appointment of an  
2 emergency manager for a municipality under PA 436 is  
3 inconsistent with those rights. This argument fails for the  
4 simple reason that this authority that the Michigan  
5 Constitution grants to municipalities is subject to state  
6 laws enacted by the legislature. The constitutional  
7 provision specifically says so. It states, quote, "Each city  
8 and village shall have the power to adopt resolutions and  
9 ordinances relating to its municipal concerns, property and  
10 government, subject to the constitution and law," close  
11 quote. Indeed, Section 1-102 of the city -- excuse me -- of  
12 the charter of the City of Detroit states, quote, "The City  
13 has the comprehensive home rule power conferred upon it by  
14 the Michigan Constitution, subject only to the limitations on  
15 the exercise of that power contained in the Constitution or  
16 this Charter or imposed by statute," close quote.  
17 Accordingly, the Court finds that PA 436 does not violate the  
18 home rule provisions of the Michigan Constitution.

19 Many objectors argue that the bankruptcy  
20 authorization section of PA 436 itself does not comply with  
21 the heightened requirements for protecting pensions in the  
22 Michigan Constitution and, therefore, that PA 436 is  
23 unconstitutional. Accordingly, the objectors argue that PA  
24 436 cannot provide a valid basis for authorization to file a  
25 bankruptcy. The Court has already explained that pension



1 benefits are a contractual obligation of the municipality and  
2 not entitled to any heightened protection in bankruptcy. It  
3 follows that if a state consents to a municipal bankruptcy,  
4 no state law can protect pension rights that are merely  
5 contractual rights from impairment in bankruptcy just as no  
6 law could protect any other type of contract rights like  
7 bonds. Accordingly, the failure of PA 436 to protect pension  
8 rights in a municipal bankruptcy does not make that law  
9 inconsistent with the pension clause of the Michigan  
10 Constitution any more than the failure of PA 436 to protect,  
11 for example, bond debt in bankruptcy is inconsistent with the  
12 contracts clause of Michigan Constitution. For this purpose,  
13 the parallel is perfect. For these reasons, the Court  
14 concludes that PA 436 does not violate the pension clause of  
15 the Michigan Constitution.

16 PA 436 permits the governor to place contingencies  
17 on a local government in order to proceed under Chapter 9.  
18 The governor chose not to impose a contingency requiring the  
19 City of Detroit to protect pensions in bankruptcy. Several  
20 objectors argue that the pension clause of the Michigan  
21 Constitution obligated the governor to include such a  
22 condition in his authorization. The Court concluded earlier  
23 that any such condition in PA 436 itself would be ineffective  
24 and potentially invalid under federal law. For the same  
25 reason, any such contingency in the governor's authorization

1 letter would have been invalid and may have rendered the  
2 authorization itself invalid under Section 109(c).

3 Accordingly, this objection is overruled. The Court  
4 concludes that the governor's authorization to file this  
5 bankruptcy case under PA 436 was valid under the Michigan  
6 Constitution.

7 On July 3, 2013, Gracie Webster and Veronica Thomas  
8 filed a complaint against the State of Michigan, Governor  
9 Snyder, and Treasurer Dillon in the Ingham County Circuit  
10 Court. They sought a declaratory judgment that PA 436 is  
11 unconstitutional because it permits accrued pension benefits  
12 to be diminished or impaired in violation of Article IX,  
13 Section 24, of the Michigan Constitution. The complaint also  
14 sought a preliminary and permanent injunction enjoining the  
15 governor and the treasurer from authorizing the Detroit  
16 emergency manager to commence proceedings under Chapter 9 of  
17 the Bankruptcy Code.

18 On Thursday, July 18th, 2013, just minutes after the  
19 city filed its bankruptcy petition, the state court held a  
20 hearing. During that hearing, the state court confirmed that  
21 the bankruptcy case had been filed. Nevertheless, the state  
22 court granted the relief enjoining the governor and the  
23 emergency manager -- excuse me -- enjoining the governor from  
24 taking any further action in the bankruptcy proceeding.

25 A further hearing was held the next day on the

1 plaintiff's request to amend the order of the previous  
2 afternoon. At the conclusion of that hearing, the judge then  
3 stated her decision to grant the declaratory relief that the  
4 plaintiffs had requested. Later that day on July 19th, 2013,  
5 the court entered a declaratory -- an order of declaratory  
6 relief. It states that PA 436 is unconstitutional and in  
7 violation of Article IX, Section 24, of the Michigan  
8 Constitution. It also states that PA 436 is to that extent  
9 of no force and effect. In their objections in this case,  
10 several of the objectors assert that this judgment precludes  
11 or prevents the city from asserting that PA 436 is  
12 constitutional or that the governor properly authorized this  
13 bankruptcy filing.

14           There are, however, two main reasons why this Court  
15 is not required to honor the Webster judgment in this  
16 bankruptcy case. First, upon the city's bankruptcy filing,  
17 federal law gave this Court exclusive jurisdiction to  
18 determine all issues relating to the city's eligibility to be  
19 a Chapter 9 debtor. At that moment, the state court no  
20 longer had jurisdiction. Accordingly, the state court's  
21 order of declaratory judgment on which the objectors rely is  
22 void and of no effect. It does not preclude the city from  
23 asserting its eligibility to file bankruptcy in this case.

24           Second, bankruptcy law provides that when a  
25 bankruptcy petition is filed, it operates as a stay of any

1 act to exercise control over property of the estate. The  
2 main objectives of the plaintiff's case in Webster v.  
3 Michigan was to protect the plaintiff's pension rights by  
4 prohibiting a bankruptcy case which might allow the city to  
5 use its property in a way that might impair pensions. It  
6 does not matter that neither the city nor its officers were  
7 defendants. The suit was clearly an act to exercise control  
8 over the city's property. Accordingly, it was stayed under  
9 the bankruptcy law. The state court's order of declaratory  
10 relief was entered in violation of the stay. For those two  
11 reasons, the Court concludes that the judgment in Webster is  
12 void, and this objection to the city's eligibility is  
13 rejected.

14 To be eligible for relief under Chapter 9, the city  
15 must establish that it is insolvent. A few objectors contest  
16 this requirement of eligibility under Section 109(c)(3). For  
17 a municipality, the Bankruptcy Code defines insolvent as,  
18 quote, "a financial condition such that the municipality is:  
19 (i) generally not paying its debts as they become due unless  
20 such debts are the subject of a bona fide dispute; or (ii) is  
21 unable to pay its debts as they become due." The Court finds  
22 that the City of Detroit was and is insolvent under both  
23 definitions. The Court has already detailed the enormous  
24 financial distress that the city faced as of July 18th, 2013,  
25 and will not repeat it here. The Court finds that the city

1 was generally not paying its debts as they became due.

2 In May 2013 the city deferred payments on \$54  
3 million in pension contributions. On July 30th it deferred  
4 an additional \$5 million fiscal year-end payment. The city  
5 also did not make a scheduled \$39.7 million payment on its  
6 COP's on June 14th. It was also spending more money than it  
7 was receiving and only making up the difference through  
8 expensive and even catastrophic borrowings. These facts  
9 establish that the city was generally not paying its debts as  
10 they became due as of the time of filing.

11 The evidence also overwhelmingly establishes that  
12 the city is unable to pay its debts as they become due. The  
13 evidence established that as a result of the city's financial  
14 state, there are many, many services in the city which do not  
15 function properly. The facts found earlier firmly support  
16 this conclusion.

17 Most powerfully, however, the testimony of Chief  
18 Craig established that the city is in a state of service  
19 delivery insolvency as of July 18th and will continue to be  
20 for the foreseeable future. He testified that the conditions  
21 in the local precincts were deplorable. He said, quote, "if  
22 I just might summarize it in a very short way, that  
23 everything is broken, deplorable conditions, crime is high --  
24 extremely high, morale is low, the absence of leadership,"  
25 close quote. He described the city as, quote, "extremely

1 violent," close quote, based on the high rate of violent  
2 crime and the low rate of clearance of violent crimes. He  
3 stated that their facilities, equipment, and vehicles were in  
4 various states of disrepair and obsolescence. Service  
5 delivery insolvency focuses on the municipality's inability  
6 to pay for all costs of providing services at the level and  
7 quality that are required for the health, safety, and welfare  
8 of the community.

9           The objecting parties assert that the city could  
10 have and should have monetized a number of its assets in  
11 order to make up for its severe cash flow insolvency. Most  
12 directly, this objection targets the city's valuable art  
13 collection. However, the city's witnesses credibly  
14 established that sales of city assets would not address the  
15 long-term operational structural financial imbalance facing  
16 the city, and this makes sense. When the expenses of an  
17 enterprise exceed its revenue, a one-time infusion of cash,  
18 whether from an asset sale or from a borrowing, only delays  
19 the inevitable financial failure unless, in the meantime, the  
20 enterprise sufficiently reduces its expenses or enhances its  
21 income. The City of Detroit itself has proven the reality of  
22 this many, many times. In any event, when considering  
23 selling an asset, the enterprise must take extreme care that  
24 the asset is truly unnecessary in pursuing its mission and  
25 unnecessary in enhancing its operational revenue. For these

1 reasons, the Court finds that the city has established that  
2 it is insolvent.

3           The city must also establish that it desires to  
4 effect a plan to adjust its debts under Section 109(c)(4).  
5 In the City of Stockton case, the Bankruptcy Court explained  
6 the cases equate desire with intent and make clear that this  
7 element is highly subjective. At the first level, the  
8 question is whether the Chapter 9 case was filed for some  
9 ulterior motive such as to buy time or to evade creditors  
10 rather than to restructure the city's finances. Several  
11 objectors assert that the city does not desire to effect a  
12 plan to adjust its debts. The Court concludes that the  
13 evidence overwhelmingly establishes that the city does desire  
14 to effect a plan in this case. Mr. Orr so testified. More  
15 importantly, before filing this case, Mr. Orr did submit to  
16 creditors a plan to adjust the city's debts. Plainly, that  
17 plan was not acceptable to any of the city's creditors. It  
18 may not have even been confirmable under the Bankruptcy Code,  
19 although that is not necessary to resolve at this time.  
20 Still, it was evidence of the city's desire and intent to  
21 effectuate a plan. There is simply no evidence that the city  
22 has an ulterior motive in pursuing Chapter 9 such as to buy  
23 time or to evade creditors. Indeed, the objecting creditors  
24 do not really contend that there was any such ulterior  
25 motive. Rather, their argument is that the plan that the

1 emergency manager has stated he intends to propose in this  
2 case is not a confirmable plan. It is not confirmable, they  
3 argue, because it will impair pensions in violation of the  
4 Michigan Constitution. Certainly the evidence does  
5 establish -- certainly the evidence does establish that the  
6 emergency manager intends to propose a plan that impairs  
7 pensions. The Court has already so found. Nevertheless, the  
8 objectors' argument must be rejected. As established  
9 earlier, a Chapter 9 plan may impair pension rights. The  
10 emergency manager's stated intent to propose a plan that  
11 impairs pensions is, therefore, not inconsistent with a  
12 desire to effect a plan. Accordingly, the Court finds that  
13 the city does desire to effect a plan.

14           The fifth element for eligibility is found in  
15 Section 109(c)(5). Under that section an entity may be a  
16 debtor under Chapter 9 if such entity has either negotiated  
17 in good faith with creditors or is unable to negotiate with  
18 creditors because such negotiation is impracticable. In the  
19 present case, the City of Detroit argues that the June 14,  
20 2013, proposal to creditors along with its follow-up meetings  
21 was a good faith effort to begin negotiations to which  
22 creditors refused to respond. The Court concludes, however,  
23 that the June 14 proposal to creditors and the follow-up  
24 meetings were not sufficient to satisfy the requirements of  
25 good faith negotiations under law. The proposal to creditors



1 did not provide creditors with sufficient information to make  
2 meaningful counterproposals, especially in the very short  
3 amount of time that the city allowed for the, quote,  
4 "discussion," close quote, period. Charitably stated, the  
5 proposal is very summary in nature. There was simply not  
6 enough information for creditors to start meaningful  
7 negotiations. For example, Brad Robins of Greenhill &  
8 Company, the financial advisor for the Retirement Systems,  
9 testified, quote, "The note itself I thought was not really a  
10 serious proposal but may be a placeholder, no maturity, no  
11 obligation for the city to pay," close quote. The city  
12 asserts that it provided supporting data in an electronic  
13 data room. However, several witnesses testified that the  
14 data room did not contain the necessary data to make a  
15 meaningful evaluation of the proposal to creditors.  
16 Moreover, the city conditioned access to the data room on the  
17 signing of a confidentiality and release agreement. This  
18 created an unnecessary hurdle for creditors. The creditors  
19 simply cannot be faulted for failing to offer  
20 counterproposals when they did not have the necessary  
21 information to evaluate the city's vague initial proposal.  
22 The proposal for creditors provided a calendar. It allotted  
23 one week, June 17 to 24, for requests for additional  
24 information. The initial rounds of discussions were  
25 scheduled for July 17 -- sorry -- June 17 to July 12, and the

1 evaluation period was scheduled to be July 15 to July 19.  
2 This calendar was very tight and did not request  
3 counterproposals or even provide a deadline for submitting  
4 them. The total time available under this schedule for  
5 creditor negotiations was approximately 30 days. Given the  
6 extraordinary complexities of the case and the 100,000  
7 creditors, that amount of time is simply far too short to  
8 conclude that such a vague proposal to creditors rises to the  
9 level required to shift the burden to objectors to make  
10 counterproposals.

11 In addition, the city affirmatively stated that the  
12 meetings were not negotiations. The city asserts that this  
13 was to clarify that the city was not waiving the suspension  
14 of collective bargaining under Public Act 436, but the city  
15 cannot announce to creditors that the meetings were not  
16 negotiations and then assert to this Court that those same  
17 meetings amounted to good faith negotiations.

18 Finally, the format of the meetings were primarily  
19 presentational, informational, to different groups of  
20 creditors with different issues and gave little opportunity  
21 for creditor input or substantive discussion.

22 Accordingly, the Court concludes that the city has  
23 not established by a preponderance of the evidence that it  
24 has satisfied the requirements for good faith negotiations.

25 Congress adopted Section 109(c)(5)(C) specifically

1 to cover situations in which a very large body of creditors  
2 would render pre-filing negotiations impracticable. Several  
3 cases suggest that the impracticability requirement must be  
4 satisfied based -- or excuse me -- may be satisfied based on  
5 the sheer number of creditors involved. The list of  
6 creditors of the City of Detroit is over 3,500 pages. It  
7 lists over 100,000 creditors. The city estimates over 20,000  
8 individual retirees are owed pension funds. The Court is  
9 satisfied that when Congress enacted the impracticability  
10 section, it foresaw precisely a situation like that which  
11 faces the City of Detroit. The sheer size of the debt and  
12 the number of individual creditors made pre-bankruptcy  
13 negotiation impracticable, impossible really.

14           There are, however, several other circumstances that  
15 also support a finding of impracticability. First, although  
16 several unions have now come forward that they are the  
17 natural representatives of the retirees, these same unions  
18 asserted in response to the city's pre-filing inquiries that  
19 they could not and did not represent retirees. These  
20 responses sent a clear message to the city that the unions  
21 would not negotiate on behalf of retirees.

22           Several voluntary associations of retirees also  
23 assert that they are the natural representatives of retirees.  
24 However, none assert that they can bind individual retirees  
25 absent some sort of cumbersome class action litigation. As

1 Donald Taylor testified, ultimately it would be up to the  
2 individual members of the association to decide if they would  
3 accept or reject an offer.

4 Further, several witnesses who testified on behalf  
5 of the retiree associations made their positions clear that  
6 they would not have negotiated a reduction in accrued pension  
7 benefits because they consider them to be fully protected by  
8 state law. It is impracticable to negotiate with a group  
9 that asserts that their position is immutable. As the Court  
10 stated in Stockton, "It is impracticable to negotiate with a  
11 stone wall."

12 Finally, the city has demonstrated that time was  
13 quickly running out on its liquidity. Accordingly, the Court  
14 finds that pre-filing negotiations were impracticable.

15 The last requirement for eligibility is set forth in  
16 Bankruptcy Code Section 921(c). That section provides,  
17 quote, "After any objection to the petition, the court, after  
18 notice and a hearing, may dismiss the petition if the debtor  
19 did not file the petition in bad faith -- excuse me -- in  
20 good faith," close quote. The city's alleged bad faith in  
21 filing its Chapter 9 petition was a central issue in the  
22 eligibility trial. Indeed, in one form or another all of the  
23 objecting parties have taken the position that the city did  
24 not file its Chapter 9 petition in good faith and that this  
25 Court should exercise its discretion to dismiss this case.

1 As will be explained, the Court finds that the totality of  
2 circumstances coupled with the presumption of good faith  
3 which arises because the city has proven each of the elements  
4 of eligibility under Section 109(c) establishes that the city  
5 filed its petition in good faith under 921(c).

6 In a moment, the Court will review the factors upon  
7 which it relies in finding that the city filed this case in  
8 bad -- in good faith. First, however, the Court considers it  
9 crucial to this process to give voice to what it understands  
10 is the narrative supporting the objecting parties' argument  
11 that the City of Detroit did not file this case in good  
12 faith. The Court will then explain why there is some support  
13 in the record for this narrative. After that, the Court will  
14 then explain why it still finds that the city filed this  
15 petition in good faith. It must be recognized that the  
16 narrative that the Court describes here is a composite of the  
17 objecting parties' presentation on this issue. No single  
18 objecting party neatly laid out this precise version with all  
19 of its features described here. Moreover, it includes the  
20 perceptions of not only several of the objecting parties  
21 whose objections were filed by attorneys, but also many of  
22 the individual objecting parties. This description does not  
23 contain the Court's findings. It is only the Court's  
24 perception of a compositive narrative -- excuse me --  
25 composite narrative that appears to ground the objectors'

1 various bad faith arguments.

2           According to this composite narrative of the lead-up  
3 to the bankruptcy filing on July 18, 2013, the City of  
4 Detroit's bankruptcy was the intended consequence of a long-  
5 term strategic plan. The goal of this bankruptcy, according  
6 to this narrative, was the impairment of pension rights  
7 through a bankruptcy filing by the city. Its genesis, the  
8 narrative goes, was hatched in a Law Review article that two  
9 Jones Day attorneys wrote. This is significant because Jones  
10 Day later became not only the city's attorneys in the case  
11 but the law firm from which the city's emergency manager was  
12 hired. The article laid out in detail the legal road map for  
13 using bankruptcy to impair municipal pensions. The objectors  
14 believe that the plan was executed by the top officials of  
15 the State of Michigan and the state's legal and financial  
16 consultants. The goals of the plan included also lining the  
17 professionals' pockets while extending the power of the state  
18 government at the expense of the people of the City of  
19 Detroit. In this narrative, there may even be a racial  
20 element to the plan. The plan participants foresaw the  
21 rejection of PA 4, according to this narrative, coming in the  
22 November 2012 election, and so work began on PA 436 even  
23 before that. As a result, it only took 14 days to enact PA  
24 436 after it was introduced in the legislature's post-  
25 election lame duck session. PA 436 was also enacted contrary

1 to the will of the people of the State of Michigan, as just  
2 expressed in their rejection of PA 4. The plan included  
3 inserting into PA 436 two very minor appropriations  
4 provisions so that the law would not be subject to the  
5 people's right of referendum and would not risk the same fate  
6 as PA 4 had just experienced. The plan also saw the value in  
7 enticing a bankruptcy attorney to become the emergency  
8 manager even though he did not have the qualifications  
9 required by PA 436. Another important part of the plan,  
10 according to this narrative, was for the state government to  
11 starve the city of cash by reducing its revenue sharing, by  
12 refusing to pay the city millions of promised dollars, and by  
13 imposing on the city a heavy financial burden of expensive  
14 professionals. It also included suppressing information  
15 about the value of the city's assets. The narrative  
16 continues that this plan also required active concealment and  
17 even deception. One purpose was to deny creditors,  
18 especially those whose retirement benefits would be at risk  
19 from such a filing, from effectively acting to protect those  
20 interests. This concealment and deception were accomplished,  
21 the narrative goes, through a public relations campaign that  
22 deliberately misstated the ultimate objective of PA 436,  
23 downplayed the likelihood of bankruptcy, asserted an unfunded  
24 pension liability amount that was based on misleading and  
25 incomplete data and analysis, understated the city's ability

1 to meet that liability, and obscured the vulnerability of  
2 pensions in bankruptcy. It also included imposing an  
3 improper requirement to sign a confidentiality and release  
4 agreement as a condition of accessing financial information  
5 in the data room. As the bankruptcy filing approached, the  
6 narrative states that a necessary part of the plan became to  
7 engage with creditors only the minimum necessary so that the  
8 Court could later assert in -- so that the city could later  
9 assert in Bankruptcy Court that it attempted to negotiate in  
10 good faith. The plan, however, was not to engage in  
11 meaningful pre-petition negotiations with the creditors  
12 because successful negotiation might thwart the plan to file  
13 a bankruptcy. "Check a box" was the phrase that some  
14 objecting parties used for this.

15           The penultimate moment that represented the  
16 successful culmination of the plan was the bankruptcy filing  
17 itself. In this narrative, this was accomplished in secrecy  
18 and a day before the planned date in order to prevent the  
19 retirees who were at that moment in state court pursuing  
20 their available state law remedies to protect their  
21 constitutional pension rights. "In the dark of the night"  
22 was the phrase used to describe the actual timing of the  
23 filing. The phrase refers to the secrecy surrounding the  
24 filing and captures in shorthand the assertion that the  
25 petition was filed to avoid an imminent adverse ruling in the



1 Webster case in state court.

2           The oft repeated phrase that was important to the  
3 objectors' theory of the city's bad faith was "foregone  
4 conclusion." This was used in the assertion that Detroit's  
5 bankruptcy case was a foregone conclusion perhaps as early as  
6 January 2013, perhaps even earlier.

7           Finally, post-petition the plan also necessitated  
8 the assertion of the common interest privilege to protect it  
9 and its participants from disclosure. The Court must  
10 emphasize again now that what the Court just summarized is  
11 what it believes is the viewpoint of the objecting parties.  
12 Those were not the Court's findings.

13           The Court will now, however, turn to its evaluation  
14 of this viewpoint of bad faith on the city's part in filing  
15 this case. The Court acknowledges that many people in  
16 Detroit hold to this narrative or at least to substantial  
17 parts of it. The Court further recognizes, on the other  
18 hand, that state and city officials vehemently deny any such  
19 improper motives or tactics as this theory attributes to  
20 them. They contend that this case was filed for the proper  
21 desire and necessary purpose of restructuring the city's  
22 debts, including its pension debt, through a plan of  
23 adjustment. Indeed, the Court has already found that the  
24 city does desire to effect a plan of adjustment. The Court  
25 finds, however, that in some particulars the record does

1 support the objectors' view of the reality that led to this  
2 bankruptcy filing. It is, however, not nearly supported  
3 enough -- in enough particulars for this Court to find that  
4 the filing was in bad faith. For example, Howard Ryan  
5 testified that the appropriations provision of PA 436 was  
6 added to evade a referendum. An e-mail from Kevyn Orr was to  
7 the same effect. The Jones Day pitch book from January 2013  
8 laid out the scenario for this bankruptcy case, and Mr. Orr  
9 was, after all, a bankruptcy lawyer, and his associates at  
10 Jones Day did write the legal road map for this back in 2011.  
11 And at the June 10 public meeting, Mr. Orr did mislead the  
12 public about the status of pensions in bankruptcy as well as  
13 about the chances of filing bankruptcy. The issue that such  
14 evidence presents, however, is how to evaluate it in the  
15 context of the good faith issue. One important question  
16 raised, for example, is during the lead-up, was the City of  
17 Detroit's bankruptcy filing a foregone conclusion as the  
18 objecting parties assert. The answer is, yes, of course it  
19 was, for a long time. Even if it was a foregone conclusion,  
20 experience with both individuals and businesses in financial  
21 distress establish that they often wait longer to file a  
22 bankruptcy than is in their interests. Detroit was no  
23 exception. Its financial crisis had been worsening for  
24 decades, and it could have and should have filed bankruptcy  
25 long before it did, perhaps even years before. Certainly the

1 Court must conclude that the bankruptcy -- that the  
2 bankruptcy filing by the City of Detroit was a foregone  
3 conclusion during all of 2013, but waiting too long does not  
4 suggest bad faith.

5 Perhaps it would have been more consistent with our  
6 democratic ideals and with the economic and social needs of  
7 the city if its officials and state officials had openly and  
8 forthrightly recognized the need for filing bankruptcy when  
9 that need first arose. It is, after all, not bad faith to  
10 file bankruptcy when it is needed, and city officials could  
11 also avoided the appearances of pretext negotiations and the  
12 resulting mistrust by simply announcing honestly that the  
13 city is insolvent, that it needs to file bankruptcy, and that  
14 negotiations would not even be attempted because it would be  
15 impracticable. The law clearly permits that and for good  
16 reason. It avoids the very delay and worse the very  
17 suspicion and bad feeling that resulted here. The Court must  
18 acknowledge some truth in the factual basis of the objectors'  
19 claim that this case was not filed in good faith.

20 Nevertheless, for strong reasons that the Court will state  
21 next, it finds that this case was filed in good faith and  
22 should not be dismissed.

23 Number one, the Court finds that the city's  
24 financial problems are of a type contemplated for Chapter 9  
25 relief. The Court's finding here is based on its finding

1 that the city is insolvent and that the city was unable to  
2 negotiate with creditors because that negotiation was  
3 impracticable.

4           Number two, the city's filings are consistent with  
5 the remedial purpose of Chapter 9. The Court's analysis on  
6 this factor is based on its finding that the city desires to  
7 effect a plan to adjust its debts. To show bad faith on this  
8 factor, the evidence must establish that the purpose of the  
9 filing of the Chapter 9 was not simply to buy time or --  
10 excuse me -- to show good faith on this factor, the evidence  
11 must establish that the purpose of the filing was not simply  
12 to buy time or evade creditors. Notably, this argument was  
13 not raised by the objectors in any pleadings or at trial, and  
14 there's no evidence. The objectors do assert that the city  
15 filed this petition to avoid a bad state court ruling in the  
16 Webster litigation. They argue this is indicative of bad  
17 faith. This argument is also rejected. It is quite common  
18 for creditor lawsuits to precipitate bankruptcy filings.  
19 That the lawsuits were in vindication of an important right  
20 under the state Constitution does not change this result.  
21 They were still suits to enforce creditors' claims against a  
22 debtor that could not pay those claims. The objectors also  
23 argue that the city filed the petition so that its pension  
24 obligations could be impaired, and this is inconsistent with  
25 the remedial purpose of bankruptcy. Again, discharging debt

1 is what motivates every debtor that files bankruptcy, and  
2 that motivation does not suggest bad faith.

3 Three, the city made efforts to improve the state of  
4 its finances prior to filing to no avail. Although the Court  
5 finds that the city did not engage in good faith negotiations  
6 with its creditors, the Court does find that the city did  
7 make some efforts to improve its financial condition before  
8 filing its Chapter 9 petition, which resulted in some  
9 savings, as stated earlier. No objecting parties have  
10 suggested any other measure that the city could have taken to  
11 relieve its financial stress other than selling assets, but,  
12 as stated earlier, that would not have solved any long-term  
13 financial problems. The fact that the city did not consider  
14 any alternatives to Chapter 9 in the period leading up to the  
15 filing does not indicate bad faith either. By that time, all  
16 of the measures that the city had attempted had largely  
17 failed to resolve the problem of the city's cash flow  
18 insolvency.

19 Four, the residents of the City of Detroit will be  
20 severely prejudiced if this case is dismissed. The Court  
21 concludes that this factor is of paramount importance in this  
22 case. The city's debt and cash flow insolvency is causing  
23 its nearly 700,000 residents to suffer hardship. As already  
24 discussed at length, the city is service delivery insolvent.  
25 Without the protection of Chapter 9, the city will be forced

1 to continue on the path that it was on until it filed this  
2 case. In order to free up cash for day-to-day operations,  
3 the city would have to continue to borrow money, defer  
4 capital investments, and shrink its workforce. This solution  
5 has proven unworkable. It is also dangerous for its  
6 residents. This factor weighs heavily in favor of finding  
7 good faith.

8           Accordingly, the Court concludes that the city's  
9 petition was filed in good faith and the petition is not  
10 subject to dismissal under Section 921(c). The Court  
11 accordingly concludes that under Section 109(c) the City of  
12 Detroit may be a debtor under Chapter 9 of the Bankruptcy  
13 Code. The Court will enter an order for relief forthwith as  
14 required by Section 921(d). The Court reminds all interested  
15 parties that this eligibility determination is merely a  
16 preliminary matter in this bankruptcy case. The city's  
17 ultimate objective is the confirmation of a plan of  
18 adjustment. It has stated on the record its intent to  
19 achieve that objective with all deliberate speed and to file  
20 a plan shortly. Accordingly, the Court strongly encourages  
21 the parties to begin to negotiate or, if they have already  
22 begun, to continue to negotiate with a view toward a  
23 consensual plan.

24           The Court recognizes and understands, to the extent  
25 it can, the widespread anguish and distress that this

1 decision to permit the city's bankruptcy to proceed may cause  
2 to the city's employees and retirees as well as their  
3 families. The Court, therefore, implores with all urgency  
4 those who administer our social safety net, our governor who  
5 authorized this case, our state government leaders, our civic  
6 and business leaders, our religious and charitable  
7 organizations, to focus yet greater attention on the real  
8 human needs that will arise because of the city's bankruptcy.

9           The message of this bankruptcy is that the city does  
10 not have enough money to properly care for its residents let  
11 alone to pay its debts, and, unfortunately, that economic  
12 fact would be true even if pensions did have the legal  
13 protection that the city's employees and retirees seek here,  
14 and that's the very wisdom of the bankruptcy law. It  
15 recognizes that people, businesses, and even municipalities  
16 can't print money, and it tries to provide an equitable and  
17 hopeful solution.

18           It is, indeed, a momentous day. We have here a  
19 judicial finding that this once proud and prosperous city  
20 can't pay its debts. It's insolvent. It's eligible for  
21 bankruptcy. At the same time, it also has an opportunity for  
22 a fresh start. I hope that everyone associated with the city  
23 will embrace that opportunity.

24           Under Section 921(e) of the Bankruptcy Code, there  
25 is no stay of this finding. The Court understands that one

1 or more parties may seek an appeal of this directly to the  
2 Court of Appeals. The Court would ask that any such request  
3 be made promptly by motion.

4 Is it still the city's intent to file a plan by  
5 year-end?

6 MR. HEIMAN: Your Honor, we're not quite certain.  
7 I'm sorry. David Heiman for the city. We're still working  
8 on our timeline but obviously mindful of your prior request  
9 that we file before March 1, so we hope to be well within  
10 that request.

11 THE COURT: All right. Thank you, sir.

12 MR. HEIMAN: Thank you.

13 THE COURT: Is there anything else that anyone would  
14 like to raise at this time? No. We'll be in recess.

15 THE CLERK: All rise. Court is in recess.

16 (Proceedings concluded at 11:33 a.m.)



## INDEX

WITNESSES:

None

EXHIBITS:

None

I certify that the foregoing is a correct transcript from the sound recording of the proceedings in the above-entitled matter.

/s/ Lois Garrett

December 5, 2013

\_\_\_\_\_  
Lois Garrett